90-130

Supreme Court, U.S.
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CLERK

No._____

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1989

AMERICAN MANUFACTURERS MUTUAL
INSURANCE COMPANY, et al.

Petitioners,

v.

UNITED STATES

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

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Dated: June 29, 1990

Questions Presented

1. Are sureties of a bankrupt South Carolina contractor liable under the Miller Act for penalties on unpaid withholding taxes?

2. Are sureties liable under the Miller Act for interest on unpaid withholding taxes of a bankrupt South Carolina contractor when the amount of the tax owed is in dispute?

3. Are sureties liable under the Miller Act for unpaid withholding taxes of a bankrupt contractor when the United States fails to institute suit to collect such taxes?

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No._____

IN THE

SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1989

AMERICAN MANUFACTURERS MUTUAL CASUALTY COMPANY, an Illinois corporation; LUMBERMENS MUTUAL CASUALTY COMPANY, an Illinois corporation; and UNITED STATES FIDELITY & GUARANTY COMPANY, a Maryland corporation,

Petitioners,

v.

UNITED STATES OF AMERICA,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

The Petitioners, American Manufacturers Mutual Insurance Company, Lumbermens Mutual Casualty Company, and United States Fidelity & Guaranty Company[1], respectfully pray that a Writ of Certiorari be issued to review the Judgment of the United States Court of Appeals for the Fourth Circuit in this case.

Opinions Below

The opinion of the Fourth Circuit (App. A, *infra*, pp. 1a-8a) has been reported at 901 F.2d 370. The opinion of the district court (App. C, *infra*, pp. 11a - 17a) has not been reported.

Jurisdiction

The judgment of the Court of Appeals (App. A, *infra*. pp. 1a-8a) was entered on March 9, 1990. A Petition for Rehearing (App. B, *infra*, pp. 9a-10a) was denied on April 6, 1990. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

Statutory Provisions Involved

The Miller Act, 40 U.S.C. § 270a(d), provides, in relevant part:

> (d) Coverage for taxes in performance bond. Every performance bond required under this section shall specifically provide coverage for taxes imposed by the United States which are collected, deducted, or withheld from wages paid by the contractor in carrying out the contract with respect to which such bond is furnished. However, the United States shall give the surety or sureties on such bond written notice,

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[1]In accordance with Rule 29.1, Supreme Court Rules, American Manufacturers Mutual Insurance Company (which is mistakenly identified in the caption as American Manufacturers Mutual Casualty Company) is neither a parent nor subsidiary of any other corporation; Lumbermens Mutual Casualty Company owns 50% or more of the stock of American Motorists Insurance Company, American Protection Insurance Company, Mico Realty Corporation, BBC Associates, Inc., KAAL PGA Sales, Inc., American Underwriting Corporation, Central Mortgage Company, Kemper Realty Corporation, Medical Audit Services, Inc., Kemper International Corporation, which owns Kemper Management Co., Ltd. (Bermuda), Kemper Insurance Co., Ltd. (Australia), Kemper, S.A. (Belgium), Kemper International Insurance Co. (PTE), Ltd. (Singapore), and The Seven Continents Insurance Co., Ltd. (Bermuda); and U S F & G Corporation is the parent corporation of United States Fidelity & Guaranty Company.

> with respect to any such unpaid taxes attributable to any period, within ninety days after the date when such contractor files a return for such period. . . No suit on such bond for such taxes shall be commenced by the United States unless notice is given as provided in the preceding sentence, and no such suit shall be commenced after the expiration of one year after the day on which such notice is given.

Statement

Merritt Dredging Company (hereinafter referred to as "Merritt") entered into several contracts with the United States Army Corps of Engineers to perform dredging services during the fourth quarter of 1983 and the first quarter of 1984 and provided the required Miller Act bonds from American Manufacturers Mutual Insurance Company, Lumbermens Mutual Casualty Company and United States Fidelity & Guaranty Company (all three hereinafter collectively referred to as "sureties").

Merritt filed its returns for its employee withholding taxes for the fourth quarter of 1983 and the first quarter of 1984 but failed to pay the taxes which it owed for either of those quarters. Subsequently, the IRS notified the sureties that they were liable for the employee withholding taxes, plus interest and penalties, as assessed by the IRS.

On April 22, 1985, the United States filed a Complaint against the sureties alleging six separate causes of action, setting forth in each a separate bonded contract and tax quarter, for the collection of unpaid employee withholding taxes, including wages that were not earned on bonded contracts, plus statutory interest and penalties. The sureties responded that they did not owe the amounts claimed as taxes and that they were not liable for interest and/or any other "statutory additions" for failure to pay taxes.

By Order, dated March 23, 1988, the Honorable C. Weston Houck, United States District Judge, held that the United States was entitled to recover unpaid taxes for employees for the time in which they were actually working on bonded jobs. The amount awarded, however, was substantially less than the amount sought by the government in its Complaint. Judge Houck held that the United States was not entitled to recover statutory interest or penalties under the provisions of the Miller Act or under South Carolina law. For some

unexplained reason, the Order provided for the government to recover taxes that were not mentioned in the Complaint. The recovery was allowed, even though the government had failed to initiate suit alleging that the taxes were due and owing.

The United States appealed that part of the District Court's decision holding that the Miller Act did not provide for the recovery from sureties of interest and penalties on unpaid employee withholding taxes. The sureties cross-appealed parts of the District Court Order, including the part of the decision finding that they were liable for unpaid employee withholding taxes which were not alleged or sought to be recovered in the Complaint filed by the government. The United States Court of Appeals for the Fourth Circuit reversed the District Court, finding that it had abused its discretion in determining that the United States was not entitled to collect interest and penalties but affirmed the judgment for taxes for which the government had not sought recovery. The Court of Appeals stated that in South Carolina a party is liable for prejudgment interest on a judgment which is in a liquidated amount and went on to hold that, therefore, the sureties were liable for both interest and statutory penalties. Even though the amount owed by the sureties was not liquidated and had been in dispute until the District Court ruled, the Court of Appeals held that the amount owed was a liquidated amount (App. A, *infra*, p. 6a). The Court simply failed to consider or address the question raised by the sureties relating to their liability for taxes on the bonded contract for which the government did not seek recovery. Petition for Rehearing was denied by the same three judge panel (App. B, *infra*, pp. 9a-10a).

Reasons for Granting the Writ

1. *In holding that the sureties are liable for penalties on unpaid withholding taxes under South Carolina law and allowing prejudgment interest on unliquidated claims, the United States Court of Appeals for the Fourth Circuit has departed from the usual course of proceedings and decided a federal question in conflict with decisions of the South Carolina Supreme Court.* Without explanation, the Court of Appeals reached the conclusion that South Carolina law allowed the award of prejudgment interest on a liquidated amount and that, therefore, the government was entitled to recover statutory penalties. The Court said:

> [T]he Miller Act requires a surety to bear the burden of compensating the government for the interest and penalties incurred on unpaid taxes when, as here, that amount is liquidated and the applicable state law allows for such recovery. [Emphasis added.] (App. A, *infra*, p. 6a)

The statement contains an obvious error. There is no applicable state law in South Carolina which allows for a recovery of penalties in addition to pre-judgment interest. Because it is apparent that the Court of Appeals erred in so holding, it should be reversed.

The only reported federal decision to address the question of whether the government is entitled to recover penalties on unpaid employee withholding taxes from sureties held that the government is not entitled to recover penalties when state law does not provide for the recovery of penalties. In concluding that the government was not entitled to recover penalties in *United Pacific Insurance Co. v. United States*, 320 F.Supp. 450 (D.Ore. 1970), the Court stated:

> The Miller Act, 40 U.S.C. § 270a(d), provides that sureties on performance bonds are liable for taxes the contractor incurs on the job, but makes no provision for penalties on those taxes.... Here, no state statute provides for recovery of penalties against a surety ...

320 F. Supp. at 452. South Carolina has no state statute or case law precedent which allows a recovery of penalties. None of the cases cited by the Court of Appeals addresses the issue of penalties. In addition, none of the cases involved the award of any amount that could be construed as interest as a penalty. Since the result reached by the Court of Appeals is without support, there is no theory under which the government is entitled to recover penalties on any taxes which the sureties may owe under a Miller Act bond.

2. *In holding that sureties are liable under the Miller Act for interest on unpaid withholding taxes when the amount of such taxes is in dispute, the United States Court of Appeals for the Fourth Circuit has decided a federal*

question of substance in a way that conflicts with decisions of the Supreme Court of South Carolina. The United States Court of Appeals for the Fourth Circuit in its decision relied on South Carolina law to allow prejudgment interest on the sureties' tax liability under Miller Act bonds "where the amount sued for is liquidated" (App. A, *infra*, p.5a). Although the amount was in dispute, the Court held that the amount owed herein was a liquidated amount in that it "became a sum certain at the time Merritt withheld income tax and FICA tax for work performed on the bonded contracts and can be calculated based on federal tax tables" (App. A, *infra*, p.5a). The Court failed to acknowledge or understand that much of the alleged tax was not covered by the bond and, as a result, the amount sued for and claimed to be owed by the government was in dispute until the District Court issued its Order. Because the government did not contest the findings of the District Court on the issue, it did not appeal that part of the decision.

The government argued to the District Court that the sureties were liable for all unpaid taxes of Merritt without regard to whether the employees involved were working on a bonded job. Because the government would not agree that the sureties were not liable for unpaid withholding taxes for employees who were paid and were not working on a bonded job, the amounts in issue were not liquidated until the District Court issued its Order resolving the amounts in dispute. As the District Court stated in its Order:

> The parties' stipulation of facts provides that "[w]hile Merritt was working on a bonded job, it would have days when no work was being performed on the contract due to either the weather or the necessity of making repairs to the dredge." Clearly, this downtime does not fall within the literal coverage of the statute and the plaintiff has failed to convince the court either that the bond should extend far enough to cover this downtime or that the wages paid during these periods were necessary "in carrying out" the bonded contract. (App. C, *infra*, pp. 16a-17a).

The United States Court of Appeals for the Fourth Circuit completely ignored this finding of fact in reversing the District Court on this issue. It is significant that the government agreed with the sureties that the

amount sought was not a liquidated amount at the District Court level when it argued in its memorandum presented to the Court that "state law plays no part in the construction of the Miller Act." This argument was made in the context, or in an effort to advance the contention, that the word "taxes" as used in the Miller Act included interest and penalties. On appeal, however, the government took a different position and contended that state law did apply so as to allow prejudgment interest.[2]

The South Carolina Supreme Court has held that, in order for a party to be entitled to prejudgment interest, the amount sued for must be a liquidated amount. In *Leaphart v. National Surety Co.*, 167 S.C. 327, 166 S.E. 415, (1932), that Court held:

> ... There is no question that interest is not recoverable on an unliquidated account... [I]nterest is allowable "if the sum is certain or capable of being reduced to a certainty, from the time when, either by the agreement of the parties or the construction of law, the payment was demandable."

166 S.E. at 421. *See also Llewelyn v. Dobson Brothers*, 274 S.C. 177, 262 S.E.2d 726 (1980); *Robert E. Lee & Co. v. Commission of Pub. Works*, 248 S.C. 92, 149 S.E.2d 59 (1966); *Southern Welding Works, Inc. v. K & S Constr. Co.*, 286 S.C. 158, 332 S.E.2d 102 (S.C.App. 1985); and *Dibble v. Sumter Ice and Fuel Co.*, 283 S.C. 278, 322 S.E.2d 678 (S.C.App. 1984).

The amount demanded and claimed due by the government was not the amount which the District Court found to be due, and at no time prior to the District Court decision did the government agree that it would accept the amount found to be due. The amount of taxes owed by the sureties, therefore, was not a liquidated amount prior to the entry of the Order of the District Court.

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[2]The government did not argue that state law would entitle it to receive penalties on the taxes although the Court of Appeals so held.

3. *In affirming the portion of the Order of the District Court that held the sureties liable for unpaid withholding taxes under the Miller Act for a bonded job on which no action was initiated to recover the unpaid taxes, the United States Court of Appeals for the Fourth Circuit has departed from the accepted and usual course of judicial proceedings and sanctioned such a departure by the District Court.* The Court of Appeals has further departed from the accepted and usual course of judicial proceedings by allowing the recovery of interest and penalties on these same withholding taxes when no action was initiated by the government on the contract. In its opinion, the Court of Appeals held that the notices received by the sureties from the government concerning tax liability under the performance bonds issued to Merritt were adequate under the Miller Act. However, it failed to address the question raised by the sureties concerning the failure of the government to commence suit on the performance bond issued for Contract Number DACW60-84-C-0002 for the fourth quarter of 1983.

The Miller Act, 40 U.S.C. § 270a(d), requires the government to file suit within one year after notice has been given that taxes are owed as a prerequisite to collecting those taxes on a performance bond. No suit was ever filed to collect taxes owed under Contract Number DACW60-84-C-0002 for the fourth quarter of 1983. Thus, the Court of Appeals' holding with reference to this contract permits a recovery which the clear wording of the statute prohibits. This precedent, if allowed to stand, would appear to authorize recovery by the government if it chooses to bring suit after the one year period set out in the statute. As a result, sureties would face uncertainty regarding liability on contracts where the government does not file suit within the one year period. The Miller Act does not permit such a result. The government is, therefore, not entitled to collect taxes under the Miller Act for Contract Number DACW60-84-C-0002 for the fourth quarter of 1983.

Conclusion

The Court of Appeals awarded penalties to the government without setting forth any legal basis for the award and failed to consider the issue of whether the government is entitled to payment of taxes on a bonded contract when it fails to initiate suit for the recovery of the taxes. Its decision as to these questions is such a departure from the accepted and usual course of judicial proceedings that it calls for the exercise of the power of supervision of the United States Supreme Court.

Furthermore, the Court of Appeals' decision regarding the award of prejudgment interest on unpaid withholding taxes, the amount of which is in dispute, is in direct conflict with the decisions of the South Carolina Supreme Court.

Substantial injustice has been done to the Petitioners, and those in the same or similar position in the future will suffer an injustice which can only be rectified by the assumption of jurisdiction of this case by this Court.

For the foregoing reasons, we ask that the Petition for a Writ of Certiorari be granted.

Respectfully submitted,

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APPENDICES

Appendix A

Opinion of United States Court of Appeals

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 88-1712

UNITED STATES OF AMERICA,

Plaintiff - Appellant,

v.

AMERICAN MANUFACTURERS MUTUAL CASUALTY COMPANY, an Illinois corporation; LUMBERMENS MUTUAL CASUALTY COMPANY, an Illinois corporation; and UNITED STATES FIDELITY & GUARANTY COMPANY, a Maryland corporation,

Defendants - Appellees.

No. 88-1724

UNITED STATES OF AMERICA,

Plaintiff - Appellant,

v.

AMERICAN MANUFACTURERS MUTUAL CASUALTY COMPANY, an Illinois corporation; LUMBERMENS MUTUAL CASUALTY COMPANY, an Illinois corporation; and UNITED STATES FIDELITY & GUARANTY COMPANY, a Maryland corporation,

Defendants - Appellees.

Appeals from the United States District Court for the District of South Carolina, at Charleston. C. Weston Houck, District Judge. (CA-85-1054-2)

Argued: January 11, 1989 Decided: March 9, 1990

Before RUSSELL and WILKINS, Circuit Judges, and KELLAM, Senior United States District Judge for the Eastern District of Virginia, sitting by designation.

Michael James Roach (William S. Rose, Jr., Assistant Attorney General, Gary R. Allen, William S. Estabrook, Tax Division, UNITED STATES DEPARTMENT OF JUSTICE; Vinton DeVane Lide, United States Attorney, on brief) for Appellant. Alice F. Paylor (ROSEN, ROSEN & HAGOOD, on brief) for Appellees.

PER CURIAM:

Pursuant to the provisions of the Miller Act, 40 U.S.C. § 270a et seq., the United States brought this action to recover for federal withholding taxes due on certain bonded government construction contracts. The named defendants were all sureties of Merritt Dredging Company, Inc. ("Merritt"), a now bankrupt construction concern, employed by the United States Army Corps of Engineers ("Army Corps") during the fourth quarter of 1983 and the first quarter of 1984 to perform dredging services. Upon motion for summary judgment, the district court ruled in favor of the United States and against the sureties. The government's recovery was limited to only that tax which had accrued under these contracts and no recovery was allowed for the penalties and prejudgment interest. An allowance of 6.71 percent rate was granted for post-judgment interest. We affirm in part and reverse in part.

I.

The taxpayer, Merritt, entered into six dredging contracts with the Army Corps. As required by the Miller Act, Merritt furnished the government with performance bonds securing its obligations.[1] These bonds were executed by the defendants United States Fidelity & Guaranty Co. ("USF&G"), Lumbermens Mutual Casualty Company ("Lumbermens"), and American Manufacturers Mutual Casualty Company ("American Manufac

[1] Section 270a(a) provides, in pertinent part:
Before any contract, exceeding $25,000 in amount, for the construction, alteration, or repair of any public building or public work of the United States is awarded to any person, such person shall furnish to the United States [secured bonds], which shall become binding upon the award of the contract to such person. . . .

turers").[2] On January 31, 1984, Merritt filed its quarterly employment tax return for the fourth quarter of 1983.. On that return, Merritt reported a total tax liability of $394,786.82.[3]

Before any of these taxes were paid, Merritt filed a petition for reorganization under Chapter 11 of the United States Bankruptcy Code, 11 U.S.C. §§ 1 et seq. In order to recover these tax dollars, the Internal Revenue Service ("IRS") moved against the sureties. The IRS sent out three letters, one dated April 24, 1984; one on June 20, 1984; and the last on June 21, 1984, informing the sureties of their tax liability.[4] In addition, the IRS asserted that each of the sureties was liable for interest and penalties accrued as a result of Merritt's non-payment.

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[2] The surety obligations on the contracts are summarized as follows:

Contract	Surety	Co-Surety	Quarter
DACW01-83-C-0105	Lumbermens	None	4th Qtr. 1983
DACW01-83-C-0112	Lumbermens	None	4th Qtr. 1983
DACW65-83-C-0056	Lumbermens	None	4th Qtr. 1983
DACW60-83-C-0032	USF&G	Lumbermens	4th Qtr. 1983
DACW01-83-C-0187	USF&G	Lumbermens	4th Qtr. 1983
DACW60-84-C-0002	USF&G	American Manufacturers	4th Qtr. 1983 1st Qtr. 1984

[3] Of this liability, $312,199.52 represented taxes withheld from the wages of its employees, including income tax and Federal Insurance Contributions Act obligations.

[4] The IRS apportioned such liability as follows:

Contract No.	4th Quarter 1983 Sureties	Amount
DACW01-83-C-0105	Lumbermens	$ 54,548.65
DACW60-83-C-0032	Lumbermens; USF&G	29,776.38
DACW65-83-C-0056	Lumbermens	14,374.78
DACW01-83-C-0112	Lumbermens	73,921.94
	TOTAL 4th Qtr.	$ 172,621.75
	1st Quarter 1984	
DACW60-84-C-0002	American Mfrs.; USF&G	$ 34,998.04
DACW01-83-C-0187	Lumbermens; USF&G	82,424.79
	TOTAL 1st Qtr.	$ 117,422.83
	TOTAL both Qtrs.	$ 290,044.58

The district court disagreed and only allowed recovery of taxes collected, deducted or withheld from wages paid when work was being performed on the contract.[5]

Both sides now appeal.

I.

We must resolve two issues: first, whether a surety, bonded pursuant to the provision of the Miller Act, may be liable to the IRS for pre-judgment interest and penalties accrued on tax money withheld by a defaulting contractor, yet not paid to the IRS when due; and, second, whether the IRS made a timely written notice to the sureties of its intent to seek payment on Merritt's delinquent tax obligation.

Pre-Judgment Interest

Under the Miller Act, whether to allow for the recovery of pre-judgment interest is a matter of federal law. *F. D. Rich Co. v. United States ex rel. Industrial Lumber Co.*, 417 U.S. 116, 127 (1974). Any decision of whether or not to award pre-judgment interest on a Miller Act Bond is committed to the sound discretion of the district court and will only be overturned upon a showing of abuse of that discretion. *United States v. Seaboard Surety Co.*, 817 F.2d 956, 965 (2d Cir. 1987). If, however, neither the Miller Act nor any other applicable federal provision provides any explicit standards for the allowance of pre-judgment interest, it is treated as incorporating the applicable state law on this issue.[6]

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[5]In calculating the amount due, the district court reviewed the dredge log books to determine exactly when Merritt was working on the bonded contracts. The logs showed that on certain dates during the fourth quarter of 1983 and the first quarter of 1984, the dredges were operating on jobs unrelated to these contracts. Accordingly, taxes withheld on these days were not included in the award to the IRS.

[6]Clearly, the Miller Act does not explicitly provide for the allowance of pre-judgment interest. We believe, however, that by allowing for recovery of taxes accrued, the Miller Act may implicate the provisions of the Federal Tax Code and its underlying policies and considerations. Because, however, we need not necessarily reach this question to resolve the matter before this court, we decline now to decide to what degree the provisions of the Miller Act and the Federal Tax Code are to be read together as compatible.

United States ex rel. Seminole Sheet Metal Co. v. SCI Inc., 828 F.2d 671, 677-78 (11th Cir. 1987); *United States ex rel. C.J.C., Inc. v. Western States Mechanical Contractors, Inc.*, 834 F.2d 1533, 1541-42 (10th Cir. 1987); *United States ex rel. Canion v. Randall & Blake*, 817 F.2d 1188, 1193 (5th Cir. 1987). We find in this case that the laws of South Carolina guide our analysis. *See United States ex rel. Weston & Brooker Co. v. Continental Casualty Co.*, 303 F.2d 91, 93 (4th Cir. 1962).[7]

South Carolina has long held that an award of prejudgment interest is to be allowed where the amount sued for is liquidated. *R. C. McEntire & Co. v. Eastern Foods, Inc.*, 702 F.2d 471 (4th Cir.), cert. denied. 464 U.S. 849 (1983); *Knight v. Sullivan Power Co.*, 140 S.C. 296, 138 S.E. 818 (1927); *Leaphart v. National Surety Co.*, 167 S.C. 327, 166 S.E. 415 (1932). The recovery sought here by the government became a sum certain at the time Merritt withheld income tax and FICA tax for work performed on the bonded contracts and can be calculated based on federal tax tables. Further, liability for payment of such taxes attached at the time the wages were paid.

The purpose of awarding pre-judgment interest is compensatory, not penal, *Rodgers v. United States*,[8] and should fairly compensate the aggrieved party. The entire structure of the Miller Act makes it clear that it was enacted to protect the United States Government from the loss it would have to bear as a result of a defaulting contractor's failure to meet all obligations. Timely payment of taxes is required by law. When such taxes are not timely paid, the government sustains a quantifiable loss that in this case can be measured by the amount withheld by Merritt for work done on the secured contracts.

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[7]Merritt was incorporated in South Carolina. Each of the sureties was licensed to do business in South Carolina and part of the dredging work was done in the state.

[8]332 U.S. 371, 373 (1947).

The recovery of interest on such delinquent funds fairly compensates the government for the loss of such monies as well as the expense incurred in retrieving it. We believe that the Miller Act requires a surety to bear the burden of compensating the government for the interest and penalties incurred on unpaid taxes when, as here, that amount is liquidated and the applicable state law allows for such recovery. The denial of that sum, if not for some other valid reason, constitutes an abuse of discretion on the part of the district court.

Notice of Tax Liability

The sureties argue that regardless of the correctness of the district court's ruling with respect to pre-judgment interest and penalties, the government failed to meet its burden of notice and accordingly is not entitled to recover any unpaid taxes from the sureties. Section D of the Miller Act provides:

> Every performance bond required under this section shall specifically provide coverage for taxes imposed by the United States which are collected, deducted, or withheld from wages paid by the contractor in carrying out the contract with respect to which such bond is furnished. However, the United States shall give the surety or sureties on such bond written notice, with respect to any such unpaid taxes attributable to any period, within ninety days after the date when such contractor files a return for such period, except that no such notice shall be given more than one hundred and eighty days from the date when a return for the period was required to be filed under Title 26. No suit on such bond for such taxes shall be commenced by the United States unless notice is given as provided in the preceding sentence, and no such suit shall be commenced after the expiration of one year after the day on which such notice is given.

This provision is to be afforded liberal construction and application in order to effectuate Congressional intent. *F.D. Rich Co. v. United States ex rel. Industrial Lumber Co., supra,* 417 U.S. at 124; *United States v. Aetna Casualty & Surety Co.*, 480 F.2d 1095 (8th Cir. 1973).

On April 24, 1984, the United States sent written notice to each of the sureties concerning taxes owed from the fourth quarter of 1983. On June 21, 1984, the United States again sent written notice concerning taxes owed for the first quarter of 1984. It is conceded that both of these letters of notification satisfied the 90-day requirement. The sureties assert, however, that these letters did not provide "notice" as required by the Miller Act in that all of the amounts stated as being owed were substantially inaccurate; the April 24, 1984, letters did not inform the sureties of the amount owed for each bond; the April 24, 1984, letter to USF&G included bonds on which it was not a surety; and the April 24, 1984, letter to USF&G omitted a contract on which the United States subsequently stated that by way of letter not within the 90-day statutory period the sureties were liable.

The purpose of the notice requirement of Section 270a(d) is to alert a surety of the principal's default on payment of its withholding taxes and that payment of the debt is expected from the surety. *United States ex rel. Jinks Lumber Co. v. Federal Ins. Co.*, 452 F.2d 485 (5th Cir. 1971). This section does not require the government to detail with specificity the contracts, bonds, and amount of delinquent taxes. All the section requires is timely notice of the contractor's default so that the surety is aware that payment from such contractor is not forthcoming. *See United States v. Fidelity & Deposit Co. of Maryland.* 690 F. Supp. 905 (D. Hawaii 1988). The fact that the timely notice contains certain factual errors and imperfections does not relieve a surety from its legal obligation to perform.

Here, it is uncontested that the government made timely notice to the sureties of Merritt's default and that taxes were due under the performance bonds. We find such notice sufficient to satisfy the requirement of Section 270a(d).[9]

[9] For this reason, we find no merit to USF&G's argument that the letter dated April 24, 1984, was insufficient notice of tax liability because it made no mention of Contract DACW60-84-C-0002. We have found no authority for the proposition that an all inclusive breakdown of tax liability is necessary when a surety is notified by the government of contractor default.

IV.

Because the notice by the government was statutorily sufficient to satisfy the requirements of the Miller Act, we find no legal obstacle to the imposition of liability for pre-judgment interest and penalties accrued as a result of Merritt's delinquency. Therefore, we find reversible error in the district court's failure to impose such liability and remand this cause for reconsideration in accordance with this opinion.

AFFIRMED IN PART, REVERSED IN PART, AND REMANDED WITH INSTRUCTIONS

Appendix B
Order of United States Court of Appeals
on Petition for Rehearing

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 88-1712

UNITED STATES OF AMERICA
Plaintiff - Appellant

v.

AMERICAN MANUFACTURERS MUTUAL CASUALTY COMPANY., an Illinois corporation; LUMBERMENS MUTUAL CASUALTY COMPANY., an Illinois corporation; UNITED STATES FIDELITY & GUARANTY COMPANY., a Maryland corporation
Defendants - Appellees

No. 88 1724

UNITED STATES OF AMERICA
Plaintiff - Appellee

v.

AMERICAN MANUFACTURERS MUTUAL CASUALTY COMPANY., an Illinois corporation; LUMBERMENS MUTUAL CASUALTY COMPANY., an Illinois corporation; UNITED STATES FIDELITY & GUARANTY COMPANY., a Maryland corporation
Defendants - Appellants

O R D E R

Upon consideration of the appellees' petition for rehearing,

Appendix B
Order of United States Court of Appeals
on Petition for Rehearing

IT IS ORDERED that the petition for rehearing is denied. Entered at the direction of Judge Russell with the concurrence of Judge Wilkins and Judge Kellam, United States District Judge sitting by designation.

For the Court,

JOHN M. GREACEN

Appendix C
Order of United States District Court

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF SOUTH CAROLINA
CHARLESTON DIVISION
CIVIL ACTION NO. 2:85-1054-2

UNITED STATES OF AMERICA,

Plaintiff,

vs.

AMERICAN MANUFACTURERS MUTUAL CASUALTY COMPANY, an Illinois corporation; LUMBERMENS MUTUAL CASUALTY COMPANY, an Illinois corporation; and UNITED STATES FIDELITY & GUARANTY COMPANY, a Maryland corporation,

Defendents

FINDINGS OF FACT, CONCLUSIONS OF LAW, ORDER, AND JUDGMENT

This is an action brought pursuant to the Miller Act, 40 U.S.C. § 270a *et seq.*, for the collection of federal withholding taxes owed by the now bankrupt employer, Merritt Dredging Company, Inc. (Merritt). The government seeks to collect these taxes from the bonding companies that provided performance bonds for contract work done by Merritt for the United States Army Corps of Engineers. The case was originally before the court on the plaintiff's motion for partial summary judgment filed October 7, 1985 and the defendants' motion for summary judgment filed October 14, 1985. On March 18, 1986, the parties filed their stipulations of fact eliminating the need for a trial in this case, and at the hearing set in this matter on July 1, 1987, counsel for both parties consented to this court's non-jury disposition of the case. The court has reviewed the pleadings, briefs, and parties' stipulation of fact in this case and now publishes the following findings of fact and conclusions of law, pursuant to Federal Rule of Civil Procedure 52(a).

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FINDINGS OF FACT

1. Merritt Dredging Company, Inc. (Merritt), was performing work under several contracts entered into with the United States Army Corps of Engineers during the fourth quarter of 1983 and the first quarter of 1984.

2. Performance bonds were executed by the Defendants, United States Fidelity & Guaranty Co. (USF&G), Lumbermens Mutual Casualty Company (Lumbermens), and American Manufacturers Mutual Casualty Company (American Manufacturers), to secure Merritt's performance pursuant to the Miller Act, 40 U.S.C. § 270a, et seq.

3. The contracts and sureties involved in this litigation are as follows:

Contract	Surety	Co-Surety	Quarter
DACW01-83-C-0105	Lumbermens	None	4th Qtr. 1983
DACW01-83-C-0112	Lumbermens	None	4th Qtr. 1983
DACW65-83-C-0056	Lumbermens	None	4th Qtr. 1983
DACW60-83-C-0032	USF&G	Lumbermens	4th Qtr. 1983
DACW01-83-C-0187	USF&G	Lumbermens	4th Qtr. 1983
DACW60-84-C-0002	USF&G	American Manufacturers	4th Qtr. 1983 lst Qtr. 1984

4. Merritt filed its quarterly tax return for the fourth quarter of 1983 on or about January 31, 1984. It did not pay the taxes that were stated to be owed in the amount of $394,786.68.

5. Merritt filed a petition for reorganization under Chapter 11 of the U.S. Bankruptcy Code on March 30, 1984.

6. By letters dated April 24, 1984, the Internal Revenue Service (IRS) informed the Defendants, USF&G and Lumbermens that each of them owed $341,247.22 in unpaid WT-FICA taxes as surety on five bonded contracts, to wit, contract Nos. DACW60-83-C-0032, DACW54-83-C-0027 (this contract was listed in the letter but no suit was brought on it), DACW65-83-C-0056, DACW01-83-C-0105, and DACW01-83-C-0112. (Exhibits "B" and "C" to Complaint).

7. By letter, dated June 20, 1984, and not within the 90-day statutory notice period, the IRS informed USF&G that it owed a total amount of

$53,495.14 as surety on two bonded contracts worked on by Merritt during the last quarter of 1983. The two contracts were contract Nos. DACW60-83-C-0032 and DACW6084-C-0002, the latter of which had not been included in the April 24 notice. This letter gave a breakdown of the taxes owed for each contract, including amounts for "Income Tax Withheld," "Employee FICA," "Interest to 7-31-84," "Failure to Pay Penalty to 7-31-84," and "Failure to Deposit Penalty." (Riddle Deposition, Defendant's Deposition Exhibit 1).

8. By letter dated June 21, 1984, and not within the 90-day statutory notice period, the IRS informed Lumbermens that it owed a total amount of $191,792.11 as surety on five bonded contracts worked on by Merritt during the last quarter of 1983. The letter stated: "The purpose of this letter is to clarify the amount due under each of the contracts, listed in our letter of April 24, 1984, for the quarter ended December 31, 1983." The letter gave a breakdown of the taxes owed for each contract, including amounts for "Income Tax Withheld," "Employee FICA," "Interest to 7-31-84," "Failure to Pay Penalty to 7-31-84," and "Failure to Deposit Penalty." (Riddle Deposition, Defendant's Deposition Exhibit 2).

9. On April 30, 1984, Merritt filed its quarterly tax return for the first quarter of 1984. It did not pay the taxes that were stated to be owed in the amount of $427,590.42.

10. By letters dated June 21, 1984, the IRS informed USF&G, Lumbermens and American Manufacturers of the taxes owed by Merritt on bonded jobs for the first quarter of 1984. These letters demanded payment by the sureties of amounts for "Income Tax Withheld," "Employee FICA," "Interest to 7-31-84," "Failure to Pay Penalty to 7-31-84," and "Failure to Deposit Penalty."

11. The figures used by the IRS in calculating the sureties' tax liability came from a worksheet prepared for the sureties and given to the IRS by Merritt, without the knowledge of the sureties. The IRS did not check the dredge log books to determine when Merritt was actually working on the bonded contracts. While Merritt was working on a bonded job, it would have days when no work was being performed on the contract due to either bad weather or the necessity of making repairs to the dredge. The employees were

still being paid and taxes for these wages are claimed by the United States as being subject to the bonds.

12. The days on which the dredges were not working are set forth in the affidavit of Victor H. Bundy, attached to Defendants' Motion for Summary Judgment.

CONCLUSIONS OF LAW

A. This court has jurisdiction of the matter under 28 U.S.C. §§ 1331, 1345.

B. The Miller Act provides in pertinent part:

> Every performance bond required under this section shall specifically provide coverage for taxes imposed by the United States which are collected, deducted, or withheld from wages paid by the contractor in carrying out the contract with respect to which such bond is furnished. However, the United States shall give the surety or sureties on such bond written notice, with respect to any such unpaid taxes attributable to any period within ninety days after the date when such contractor files a return for such periods, except that no such notice shall be given more than one hundred and eighty days from the date when a return for the period was required to be filed under Title 26. No suit on such bond for such taxes shall be commenced by the United States unless notice is given as provided in the preceding sentence, and no such suit shall be commenced after the expiration of one year after the day on which such notice is given.

40 U.S.C. § 270a(d).

C. The purpose of the notice requirement found in section 270a(d) is to alert the surety that the contractor is in default on its withholding taxes and that payment will be expected from the surety. *Accord United States for Use and Benefit of Jinks Lumber Co. v. Federal Insurance Co.*, 452 F.2d 485, 487-88 (4th Cir. 1971).

D. Section270b(a)which applies to performance bonds for the protection of subcontractors and materialmen requires that notice to the general contractor state with "substantial accuracy" the amount claimed. This specificity requirement allows the general contractor and its surety to plan for the potential liability. When Congress added subsection (d) to section 270a in 1966, however, it did not include a specificity requirement like that found in 40 U.S.C. § 270b(a). While the defendants would have the court read in such a requirement, such construction is inconsistent with the maxim *inclusio unius est exclusio alterius. See, e.g., Russello v. United States,* 464 U.S. 16, 23 (1983) (quoting *United States v. Wong Kim Bo,* 472 F.2d 720, 722 (5th Cir. 1972)). Thus, this court concludes that the government's alleged failure to be substantially accurate with the amounts set forth in the written notices is not fatal to its action to collect the taxes under 40 U.S.C. § 270a(d).

E. The notice required by 42 U.S.C. § 270a(d) is to be given "within ninety days after the date when such contractor files a return for such period ...." Merritt filed its quarterly tax return for the fourth quarter of 1983 on or about January 31, 1984. By letter dated April 24, 1984 and delivered within the 90-day period, the IRS gave notice to USF&G and Lumbermens of the unpaid taxes of Merritt for the fourth quarter of 1983. The IRS did not, however, give direct written notice to American Manufacturers, a co-surety of Merritt on contract number DACW60-84-C-0002, within the 90-day period. Nevertheless, the IRS contends that it did make an effective, timely service on American Manufacturers through its service of Lumbermens since both corporate entities are members of the Kemper Group. While it comes as no surprise that actual notice is sufficient to satisfy the statute, *see, e.g., United States ex rel. Hillsdale Rock Co., Inc. v. Cortelyou & Cole, Inc.,* 581 F.2d 239 (9th Cir. 1978), the plaintiff has not shown that notice to Lumbermens is actual notice to American Manufacturers; it is doubtful that Lumbermens and American Manufacturers share the same office and personnel as in *United States v. Barlows Commercial Const. Co.,* 567 F. Supp. 464 (D.S.C. 1983), simply because they are both members of the Kemper Group. Thus, the court now concludes that the notice to American Manufacturers for the fourth quarter 1983 taxes was untimely and ineffective.

F. Also at issue in this case is the meaning of the word "taxes" as used in the Miller Act provision requiring that "[e]very performance bond ...

shall specifically provide coverage for taxes imposed by the United States ...." 40 U.S.C. § 270a(d). The plaintiff points to the tax code which provides that "[a]ny reference in this title to 'tax' ... shall be deemed also to refer to the additions to the tax, additional amounts, and penalties provided by this chapter." 26 U.S.C. § 6662(a)(2) (emphasis added). Thus, the plaintiff avers that the Miller Act bond shall provide coverage for not only the initial tax liability but also all penalties and statutory accruals as well. This court disagrees.

In the tax code provision relied on by the plaintiff, Congress expressly limited their definition of "tax" to references in the tax code. Again, the maxim of construction *inclusio unius est exclusio alterius* would prohibit the court from reading the tax code definition into the Miller Act which is not codified as part of the tax code, Title 26. Moreover, the Act's provision requiring coverage for taxes limits the scope of those taxes to those "collected, deducted, or withheld from wages ...." 40 U.S.C. § 270a(d). The penalties and statutory accruals imposed on the employer for its failure to make timely payment of withholding taxes may not be "collected, deducted, or withheld from [employee] wages ...." *Accord* 26 U.S.C. § 3402(a)(l) (only authorizing employer to withhold tax as prescribed by the Secretary of the Treasury); *see, e.g.*, 26 C.F.R. § 301.6672-1 (1986) (specifying that the penalties for failing to pay over withholding taxes imposed by 26 U.S.C. § 6672 apply to the person required to collect, account for, and pay over such taxes).

G. Finally, the parties seek a judicial determination of whether the withholding taxes due on wages paid to Merritt employees for time not actually spent dredging on the bonded contracts are covered by the bond. The statute states that the bond shall cover "wages paid ... in carrying out the contract with respect to which such bond is furnished." 42 U.S.C. § 270a(d) (emphasis added). The bonds themselves have similar language obviously drafted to track the statute.

The parties' stipulation of facts provides that "[w]hile Merritt was working on a bonded job, it would have days when no work was being performed on the contract due to either bad weather or the necessity of making repairs to the dredge." Clearly, this down-time does not fall within the literal coverage of the statute and the plaintiff has failed to convince the court either that the bond should extend far enough to cover this downtime or that the

wages paid during these periods were necessary "in carrying out" the bonded contract.

ORDER AND JUDGMENT

IT IS THEREFORE ORDERED that the plaintiff shall have judgment against the following sureties in the specified amounts:

Contract	Judgment Against	Amounts
DACW01-83-C-0105	Lumbermens	$44,893.25
DACW60-83-C-0032	USF&G and Lumbermens, jointly and severally	$23,478.87
DACW65-83-C-0056	Lumbermens	$11,001.92
DACW01-83-C-0112	Lumbermens	$66,181.95
DACW60-84-C-0002	USF&G (only)	$12,880.01
DACW60-84-C-0002	USF&G and American Manufacturers, jointly and severally	$19,511,96
DACW01-83-C-0187	USF&G and Lumbermens, jointly and severally	$43,505.91

together with the costs of this action and post-judgment interest as provided by law.

AND IT IS SO ORDERED.

C. Weston Houck
United States District Judge

Dated:

At Florence, South Carolina
March 22, 1988